Fiscal Note 2009 Biennium

GOVERNOR'S OFFICE OF BUDGET AND PROGRAM PLANNING

Bill #	HB0618		**Title:**	Establish statewide account for employee termination costs
Primary Sponsor:	Sinrud, John		**Status:**	Third Reading

- ☐ Significant Local Gov Impact
- ☑ Needs to be included in HB 2
- ☑ Technical Concerns
- ☐ Included in the Executive Budget
- ☐ Significant Long-Term Impacts
- ☐ Dedicated Revenue Form Attached

FISCAL SUMMARY

	FY 2008 Difference	FY 2009 Difference	FY 2010 Difference	FY 2011 Difference
Expenditures:				
General Fund	$1,000,000	$2,016,500	$2,091,368	$2,117,183
State Special Revenue	$0	$7,044,861	$7,299,083	$7,156,768
Federal Special Revenue	$0	$748,701	$776,498	$786,083
Other	$0	$578,995	$600,492	$607,904
Revenue:				
General Fund	$0	$0	$0	$0
State Special Revenue	$1,057,500	$5,039,216	$5,201,137	$5,246,950
Federal Special Revenue	$0	$0	$0	$0
Other	$0	$0	$0	$0
Net Impact-General Fund Balance	($1,000,000)	($2,016,500)	($2,091,368)	($2,117,183)

Description of fiscal impact:

Under this bill agencies will be required to fund the compensated absences from vacation and sick leave pay-outs on an on-going basis, which will impact their management of personal services costs.

FISCAL ANALYSIS

Assumptions:

Department of Administration

1. An assumption is made that all employees will receive an annual 3% pay raise over the next two biennia.
2. Comparing FY 2005 & FY 2006 summary termination payouts according to the CAFR report, the average payout percentage of vacation and sick leave is approximately 1.23% of regular pay. Based on the payout

percentage and regular pay projections for FY's 2007, 2008 and 2009 this rate would need to be adjusted in FY 2010 and 2011 to 1.16%.

3. The Human Resources Standards and Services (HRSS) program within the State Personnel Division has gathered research data regarding the potential for baby boomer retirement trends. The data indicates the State of Montana retirement rate could likely increase from a current annual 2.5% to at least 3.75% over the next five years. For purposes of this fiscal note the average projected retirement rate is increased .25% each year to FY 2011. It is assumed that this increase in the retirement rate due to the above referenced baby boomer trends will eventually peak in the next ten years and start to decline.
4. The average attrition rate for state government has been steady at 12% for a number of years. The current annual retirement rate (2.5%) is included in the attrition rate. This fiscal note assumes that attrition from factors other than retirement will remain constant through time. The overall annual attrition rate will be increased by the gradual increase of the retirement rate described in assumption #3. Operating costs for the special revenue fund are absorbed into the total dollars that must be collected from agencies for vacation and sick leave payouts.
5. Fees charged to agencies to fund the termination pool are calculated based on the average of the prior three fiscal year's attrition rates for payout of unused sick and vacation leave credits as provided in 2-18-618(6) and 2-18-617(2), MCA, respectively. No other additional compensation will be paid out of the termination pool established by this bill. The fee will be applied as a percentage of gross salary (similar to how UI and Worker's Compensation taxes/fees are calculated) on only those employees who are in a work status that is eligible for accrual of sick and vacation leave credits. For example, short-term workers do not earn sick and vacation leave credits and agencies would not be charged for contributions to the termination based on these employees' gross salaries. In addition, since 2-18-617(2)(a), MCA, limits the total annual vacation leave that may be accumulated to a total not to exceed two times the maximum number of days earned annually as of the end of the first pay period of the next calendar year, the termination pool will only accumulate vacation leave payouts up to the maximum allowed by law for each individual employee. The termination pool fee will be programmed into the biweekly payroll process and automatically collected from the appropriate agencies and funds through the on- and off-cycle pay journals. Under this bill, the funding for leave payouts is calculated from current and historic pay data in current dollar amounts, whereas payouts will occur in future dollars amounts in affect at the time an employee terminates.
6. Calculations for payroll taxes have not been factored into the calculations due to the varying tax rat that could be applied. Those amounts would be over and above the amounts reflected in this fiscal note.
7. The calculations referred to in assumptions 1-5 are depicted in Table A.

Table A	FY 2005 (Actual)	FY 2006 (Actual)	FY 2007 (Projected)	FY 2008 (Projected)	FY 2009 (Projected)	FY 2010 (Projected)	FY 2011 (Projected)
Regular Salary	$367,647,677	$390,804,606	$406,436,790	$418,629,894	$431,188,791	$444,124,454	$457,448,188
Percent increase in regular salary		6.3%	4.0%	3.0%	3.0%	3.0%	3.0%
Baseline Termination Pay for sick and vacation leave - assuming a 12% total annual attrition rate, 2.5% of which is retirements	4,514,267	4,787,448	4,999,173	5,149,148	5,303,622	5,151,844	5,306,399
Termination pay for sick and vacation leave - projecting a graduated increased retirement rate component of .25% each year to FY 2011			5,011,670	5,174,893	5,343,399	5,203,362	5,372,729
Projected attrition rate	12.00%	12.00%	12.25%	12.50%	12.75%	13.00%	13.25%
3 year average attrition rate				12.1%	12.3%	12.5%	12.8%
Fees Charged to Agencies				0	4,991,337	5,176,654	5,240,552

8. A $1 million general fund transfer to the state special revenue fund will occur on July 1, 2007. The cash will be invested with a long term investment return of 5.75%. Interest earnings are retained by the state special revenue fund. Interest earnings in Table B below are based on an average mid-year investment

balance which is calculated using the addition of projected semi-annual fee revenues, termination payouts, and operating costs.

9. The state special revenue fund will receive an actuarial assessment in each even numbered year of the biennium at a projected cost of $20,000. These assessments will begin in FY 2010.
10. SABHRS system modifications to handle the collection of the agency fees described in assumption #5 above are assumed to be minimal and can be absorbed into current operating levels.
11. Central payroll would require 1.00 FTE beginning in FY 2009 to manage the activity in the termination pool. The FTE would be a Payroll Specialist with personal services cost of $47,021 in FY 2009; $48,429 in FY 2010; and $49,657 in FY 2011. In FY 2009 there will be one-time-only cost of $2,300 to set up an office workstation for this FTE. Ongoing annual operating costs are assumed to be $5,000 to support the operating functions provided by this FTE.
12. Table B summarizes the investment balances in the termination pool, revenues and expenses.

Table B	FY 2005 (Actual)	FY 2006 (Actual)	FY 2007 (Projected)	FY 2008 (Projected)	FY 2009 (Projected)	FY 2010 (Projected)	FY 2011 (Projected)
Beg of Year Investment				$1,000,000	$1,057,500	$700,240	$637,488
Interest Earnings				57,500	49,123	37,385	31,284
Fee Revenue				0	4,991,337	5,176,654	5,240,552
Personal Services and Operating Expenses				0	(54,321)	(73,429)	(54,657)
Termination Payouts				0	(5,343,399)	(5,203,362)	(5,372,729)
End of Year Investment				$1,057,500	$700,240	$637,488	$481,938

13. Annual funding of the termination pool by agency and fund type will be allocated using the following percentages: General fund – 40.4%; State Special Revenue fund – 33%; Federal Special Revenue fund – 15%; and Other funds – 11.6%.

	FY 2008 Difference	FY 2009 Difference	FY 2010 Difference	FY 2011 Difference
Fiscal Impact:				
FTE	0.00	1.00	1.00	1.00
Expenditures:				
Personal Services - FTE	$0	$47,021	$48,429	$49,657
Personal Services - Agency f	$0	$4,991,337	$5,176,654	$5,240,552
Operating Expenses	$0	$7,300	$25,000	$5,000
Termination Payouts	$0	$5,343,399	$5,203,362	$5,372,729
Transfers	$1,000,000	$0	$0	$0
TOTAL Expenditures	$1,000,000	$10,389,057	$10,453,445	$10,667,938
Funding of Expenditures:				
General Fund (01)	$1,000,000	$2,016,500	$2,091,368	$2,117,183
State Special Revenue (02)	$0	$7,044,861	$6,985,087	$7,156,768
Federal Special Revenue (03)	$0	$748,701	$776,498	$786,083
Other	$0	$578,995	$600,492	$607,904
TOTAL Funding of Exp.	$1,000,000	$10,389,057	$10,453,445	$10,667,938
Revenues:				
General Fund (01)	$0	$0	$0	$0
State Special Revenue (02)	$1,057,500	$5,039,216	$5,201,137	$5,246,950
Federal Special Revenue (03)	$0	$0	$0	$0
Other	$0	$0	$0	$0
TOTAL Revenues	$1,057,500	$5,039,216	$5,201,137	$5,246,950
Net Impact to Fund Balance (Revenue minus Funding of Expenditures):				
General Fund (01)	($1,000,000)	($2,016,500)	($2,091,368)	($2,117,183)
State Special Revenue (02)	$1,057,500	($2,005,645)	($1,783,950)	($1,909,818)
Federal Special Revenue (03)	$0	($748,701)	($776,498)	($786,083)
Other	$0	($578,995)	($600,492)	($607,904)

Technical Notes:

1. The bill calls for a transfer of $1 million into the state special revenue fund from the general fund, however, per data reported in the CAFR total termination vacation and sick leave payouts have averaged approximately $4.8 million annually. Along with the nation, HRSS has researched the potential for baby boomer retirement trends, and in light of this research it can be estimated that the retirement rate will climb from 2.5%, as it is currently, to peak at 3.75% (or greater) over the next decade or so. State agencies will make payments into the termination pool on a regular basis at a rate which lags behind the rate of termination payouts. Depending on the trend of retirements and other reasons for terminations these two rates will criss-cross with each other. New Section 2 (1) of HB 618 bases agency fees on the average of the past three years experience, therefore in periods of increasing retirement rates, such as the baby boom bubble anticipated over the next decade or so, the fund will be collecting less money than it will pay out. This trend should stabilize as time goes on and eventually the cash flow of funds in and out of the termination pool can be expected to net each other out. However, it does not appear that diverting only $1

million in general fund dollars into the termination pool special revenue fund will be sufficient to maintain a positive fund balance at FYE 2011.

2. Alaska and Utah have both developed similar fund types. Their rates are based on past experiences and the federal government has not had issues with their methodology. An actuarial assessment would not be necessary due to the straight forward rate calculations.

Sponsor's Initials	*Date*	*Budget Director's Initials*	*Date*